

STATE OF HAWAII
EMPLOYEES' RETIREMENT SYSTEM

City Financial Tower
201 Merchant Street, Suite 1400
Honolulu, Hawaii 96813-2980

CONTRIBUTORY PLAN
INFORMATION FOR PROSPECTIVE RETIREES
SUPREME, INTERMEDIATE APPEALS, CIRCUIT, DISTRICT & DISTRICT FAMILY COURT
JUDGES

August 2004

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This handout offers general information on pre-retirement issues to help you prepare for your retirement. It is only a summary and does not constitute a legal document or contract and is subject to change. Nothing contained herein shall be construed to amend, modify, override, or nullify a state statute, rule, policy, procedure or document used in the retirement process.

You are encouraged to attend a Pre-Retirement Session coordinated by your Personnel Office or to schedule a counseling session at the nearest ERS office when you are ready to file an application to retire.

* This information is available in an alternate format. Please call 586-1735 for information.

RETIREMENT ELIGIBILITY REQUIREMENTS

SERVICE RETIREMENT

(Regular or Vested/Deferred Retirement)

“Judge”: a justice of the Supreme Court, a judge of the intermediate appellate court, a judge of the circuit court, a judge of the district court, or a district family court judge of this State.

Hired as a Judge Before July 1, 1999

- 10 years of service regardless of age

Hired as a Judge After June 30, 1999

- Age 55 with a minimum of 5 years of combined Contributory and Noncontributory Plan service or 25 years of combined Contributory and Noncontributory Plan service with an age reduction if under age 55.

If the member is below age 55, benefits are computed as though age 55 was attained, then reduced 5% for each year below 55, 4% for each year below 50, 3% for each year below 45; and 2% for each year thereafter.

DISABILITY RETIREMENT

Ordinary Disability Retirement

- 10 or more years of service
- No minimum age
- Unable to work due to illness or injury (unrelated to work)
- Employment must not be terminated at time application is filed
- Benefit computed at 3½% plus annuity

Service Connected Disability Retirement

- No minimum service requirement
- No minimum age requirement
- Must be permanently disabled due to an accident on the job (which was not due to willful negligence)
- Application must be filed within two years of the accident or the date worker's compensation benefits stop

Note: Unused sick leave credits cannot be used to meet any eligibility requirements.

“PAPER RETIREMENT” PROVISIONS

Retirement benefits under Act 90/71- Sections 88-61(c) and 88-73(4)

Any judge, after attaining an allowance of 75% of the average final compensation (AFC), may elect to retire “on paper” and continue in service as a judge. Judges may also elect not to retire “on paper” and continue membership in the ERS.

“Paper Retirement” – Discontinued Membership:

- May be filed when the 75% AFC limitation is attained.
- Effective date of retirement is the day election to retire is made and the 30- to 150-day filing requirement does not apply.
- AFC will be based on salaries earned up to the date the election to retire is made even if the salary at the point of actual retirement is much higher.
- Designated beneficiary will be protected under the retirement option selected.
- No pension payment until employment actually terminates.
- Any excess contributions on account due to the 75% AFC limitation will be refunded when the election to retire is made.
- No retirement contributions will be deducted from future salary.
(Example: $\$8,910 \times 7.8\% = \694.98 per month)
- Monthly retirement allowance will commence upon termination of service. Benefits are not retroactive.
- Post retirement shall accrue until actual retirement. Thus, if termination is 10 years after election to retire is made, the initial post retirement shall be 25% ($2\frac{1}{2}\%$ per year \times 10 years) of the retirement allowance.
- Election to retire shall be irrevocable.

No “Paper Retirement” – Continued Membership:

- Contributions to the ERS will continue and federal income taxes will be deferred on all retirement contributions.
- Benefit calculation will be based on the AFC for the highest three or five years of service.
- Excess contributions will be refunded upon retirement.

Employees' RETIREMENT SYSTEM CHECKLIST

MONTHS Before Retirement	WHAT TO DO	CONTACT	DETAILS
15 months or more	Attend a Pre-Retirement Session	Your Own Department Personnel Office for schedule	An ERS representative will discuss the retirement application process, option selections, and answer any questions.
12 months	Request a Retirement Estimate <i>ERS generated estimates cannot be provided earlier than 12 months in advance of your retirement date.</i>	Call the ERS on Oahu, Hawaii, Kauai or Maui	<u>Information Needed</u> <ul style="list-style-type: none"> • Name • Social Security number • Address • Birth date • Retirement date (definite or tentative) • Monthly gross salary • Beneficiary name and birth date Any previous service, military, or maternity leaves to be acquired.
7 months	Request a Retirement Packet	Same as above	The packet will include retirement forms and instructions for completing them.
6 months	Schedule a counseling appointment with a Retirement Claims Examiner (RCE)	The ERS office nearest you	Bring your retirement packet and your spouse (recommended). During the appointment, the Retirement Claims Examiner will help you complete your retirement application; answer any questions or concerns regarding your retirement estimate; and enable you to select the best option for you and your family. Your Health Fund enrollment and tax withholding may also be completed at this time.
Not more than 150 days and not less than 30 days before retirement. Your retirement date must be the first of the month except for December, when retirement is on the first or the last day of the month.	File your Retirement Application	Notarized Applications may be hand-delivered or mailed to the ERS	<u>Required documents:</u> <ol style="list-style-type: none"> 1. Proof of birth date for you and your beneficiary (for survivor options). (Original documents only. Photocopies not accepted). <p><i>*Note: Substitutions listed below*</i></p> <ol style="list-style-type: none"> 2. A copy of your bank deposit slip or account numbers for electronic deposit of pension checks. 3. Medicare card, if applicable, for you and your spouse required by law for integration with EUTF coverage and for Medicare premium reimbursement. 4. Driver's license or State ID for signature validations.

Substitute any two of the following original documents with birth date or age in place of a certified birth certificate:

- | | |
|---|--|
| <input type="checkbox"/> Valid Hawaii Driver's License | <input type="checkbox"/> Military Record |
| <input type="checkbox"/> Hawaii State Identification Card | <input type="checkbox"/> Hospital Treatment Records |
| <input type="checkbox"/> Passport (U.S. or foreign) | <input type="checkbox"/> Life Insurance Policy |
| <input type="checkbox"/> Marriage Record | <input type="checkbox"/> School Record (with age) |
| <input type="checkbox"/> Naturalization Record | <input type="checkbox"/> Child's birth certificate (with member's age) |
| <input type="checkbox"/> Voter Registration Record | <input type="checkbox"/> Original Baptismal Certificate/Religious record |
| <input type="checkbox"/> Census Record | <input type="checkbox"/> recorded after age 5 |

FILING YOUR APPLICATION FOR RETIREMENT

A member can file only three service retirement applications. The first two service retirement applications may be cancelled prior to their effective date; however, retirement is mandatory on the third application.

You must also notify your department to determine your “close of business” (COB) date as well as your retirement date. Your last day on the payroll is your COB date. Your retirement date must be the 1st of the month except December, which can be the 1st or 31st. Your COB date and retirement date cannot be the same.

Retirement applications must be notarized. *Notary services are provided at all ERS locations at no charge.*

ERS must provide written notification of a member's retirement date, option selection, and beneficiary designation to the member's spouse/reciprocal beneficiary.

PENSION CHECK INFORMATION

Make plans to cover expenses for your first four weeks of retirement. Your first pension check will be retroactive to your retirement date and is mailed to your home 4 weeks after you retire. Your pension amount is based on the option you selected according to the latest estimate provided to you by the ERS. **You must sign up for the direct deposit of your pension check into a financial institution.**

Payment

Your first pension check is issued approximately **4 weeks** after your retirement date pending verification of your “close of business date” (last day on the payroll) by your personnel office. Your pension checks will be initially sent to your mailing address for approximately two pay periods before the direct deposit into your financial institution (if you requested it) is activated. You will receive a monthly pension, which will be paid at the end of the month.

Final Pension Adjustment

Your estimated pension will be finalized following the receipt and review of your payroll department's audited report of any unused sick leave credits and the amount of your vacation pay. Your pension will be adjusted to an exact amount retroactive to your retirement date.

Effective January 1, 2004, ERS is required to pay 4-1/2% interest per annum for pensions not finalized within 6 months after the retirement date.

Taxation of Benefits

Pension allowances are subject to federal taxes only.

Financial Institution Changes

Financial institution changes must also be requested in writing with the institution's change form from our office. Please be advised that two pension checks are mailed to your home before any changes to the financial institution becomes effective.

Choosing A Retirement Plan Option

One of the most important decisions you will make as you plan to retire is to select your retirement option. Option choices are designed to meet a range of retirement needs and goals. Pension payments continue for the retirant's lifetime for all options. However, **a beneficiary will continue to receive a pension** in the event of the retirant's death **only under Options 2, 3, Four (Five & 2), and Four (Five & 3).**

OPTION COMPARISON SUMMARY				
OPTION	Lifetime Benefit to Retiree	Lifetime Benefit to Beneficiary	Refund of Contributions	Refund Amount
Maximum Allowance	Yes	No	No	
Option One	Yes	No	No	
Option Two	Yes	Yes (100%)	No	
Option Three	Yes	Yes (50%)	No	
Option Four (Five & Max)	Yes	No	Yes	Pre-1987, 50% or 75%
Option Four (Five & 1)	Yes	No	Yes	Pre-1987, 50% or 75%
Option Four (Five & 2)	Yes	Yes (100%)	Yes	Pre-1987, 50% or 75%
Option Four (Five & 3)	Yes	Yes (50%)	Yes	Pre-1987, 50% or 75%
Option Five	Yes	No	Yes	100%

Notes:

- Changes in retirement option selections are permissible prior to the effective date of retirement; however, the law prohibits any changes thereafter.
- In the event a member dies after filing a retirement application, the death benefit is payable under the option selected.
- For Options 2 and 3 or combinations with Options 4 (Five & 2) or 4 (Five & 3), should your beneficiary predecease you after you retire, another beneficiary cannot be named.

OPTIONS WITH NO REFUND

The following options offer higher monthly pension benefits because member's contributions are not refunded.

Maximum Allowance - Highest lifetime monthly pension (for retirant's lifetime only)

- No continuing pension benefit for survivor
- No refund of contributions
- Trust, Estate, or multiple beneficiaries possible with changes allowed after retirement

Option One - Reduced lifetime monthly pension (with short-term insurance)

- No refund of contributions
- Short-term (not lifetime) insurance (coverage depletes after approximately ten years)
- Large benefit if death occurs shortly after retirement
- Trust, Estate, or multiple beneficiaries possible with changes allowed after retirement

Option Two - Lifetime reduced pension for retiree with 100% continuing pension to beneficiary in the event of retiree's death

- No refund of contributions
- Beneficiary cannot be changed after retirement

Option Three - Lifetime reduced pension for retiree with 50% continuing pension to beneficiary in the event of retiree's death

- No refund of contributions
- Beneficiary cannot be changed after retirement

REFUND OPTIONS

The following options allow the following choices of refunds of member's contributions:

- Nontaxable pre-1987 contributions
- 50% refund of contributions
- 75% refund of contributions
- 100% refund of contributions (Option Five only)

Option Four (5 & Maximum) - Highest pension for retiree's lifetime with refund

- Trust, Estate, or multiple beneficiaries and change allowed after retirement for final prorated pension check

Option Four (5 & 1) - Reduced monthly pension for retiree's lifetime with refund

- Short term insurance reserve (see Option One)

Option Four (5 & 2) - Reduced monthly pension for retiree's lifetime with refund and 100% continuing benefit for beneficiary

- Beneficiary cannot be changed (see Option Two)

Option Four (5 & 3) - Reduced lifetime monthly pension for retiree's lifetime with refund and 50% continuing benefit to beneficiary

- Beneficiary cannot be changed (see Option Three)

Option Five - Lowest monthly pension for retiree's lifetime with maximum refund of contributions and no continuing benefit for beneficiary

- 100% refund of contributions (and interest) with possible tax consequences
- Estate, Trust, or multiple beneficiaries and changes allowed after retirement for final prorated pension check

PENSION BENEFIT COMPUTATION

For each year of service as a judge, 3½% of the member's average final compensation **plus** an annuity on the contributions made while employed as a judge.

The maximum benefit is 75% of member's average final salary. If the 75% limitation is exceeded, the member is refunded the contributions in excess of the requirements. This refund is applicable only to contributions derived from service in this capacity.

The following hypothetical examples will help illustrate the Maximum Allowance calculation process:

Example 1:

- Age 54
- 10 years of service as a judge
- \$106,921.00 average annual compensation
- \$80,000.00 judge contributions plus interest

Formula:

$$\begin{aligned} 10 \text{ years} \times 3 \frac{1}{2}\% \times \$106,921.00 &= \$37,422.00 \\ \text{Plus annual annuity} &= \underline{7,848.00} \\ (\$80,000.00/10.1936) \\ \text{Maximum annual pension} &= \$45,270.00 \quad (\$3,772.00 \times 12 \text{ months}) \end{aligned}$$

Example 2:

- Age 55
- 15 years of service as a general employee
- 12 years of service as a judge
- \$106,921.00 average annual compensation (AFC)
- \$220,000.00 total contributions (General Employee: \$120,000 + Judge: \$100,000)

Formula:

$$\begin{aligned} 15 \text{ years} \times 2\% \text{ or } .30 \\ 12 \text{ years} \times 3 \frac{1}{2}\% \text{ or } .42 \\ .72 \times \$106,921.00 &= \$76,983.00 \\ \text{Plus annual annuity } (\$100,000.00/10.4849) &= \underline{+ 9,537.00} \\ &= \$86,520.00 \\ \text{Less Maximum Pension } (75\% \times \$106,921.00) &= \underline{- 80,190.00} \\ \text{Excess Benefit} &= \$6,330.00 \\ \text{Excess contributions } (\$6,330.00 \times 10.4849) &= \$66,369.42 \end{aligned}$$

Summary:

- Maximum allowance payable = 75% of AFC or \$80,190.00
- Excess contribution to be refunded = \$66,369.00
- Balance of the member's contributions (refund plans) = (\$220,000.00
- -\$66,369.00) = \$153,631.00.
- If the excess is more than \$100,000.00, the refundable amount would be restricted to that amount. The balance of the contributions (\$120,000.00) would be refundable under Options 4 or 5.
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SAMPLE RETIREMENT ESTIMATE

STATE OF HAWAII
EMPLOYEES' RETIREMENT SYSTEM
201 Merchant Street, Suite 1400
Honolulu, Hawaii 96813-2980

CONTRIBUTORY PLAN

Your estimated service retirement benefits are based on the following:

RETIREMENT DATE Mo/Day/Yr	EARNED SERVICE	23YRS 9MOS
BIRTH DATE Mo/Day/Yr (Age: 57)	ACQUIRED SERVICE	2YRS 0MOS
MEMBERSHIP DATE Mo/Day/Yr	UNUSED SICK LEAVE**	YRS MOS

BENEFICIARY	TOTAL MEMBERSHIP SERVICE	25YRS 9MOS
BIRTH DATE Mo/Day/Yr (Age: 59)		

RETIREMENT OPTION	MONTHLY PENSION			REFUND	
	RETIREE	BENEFICIARY	INSURANCE RES	AMOUNT	PERCENTAGE
Maximum Allowance	\$5,625.00	NONE	---	---	---
One	\$5,478.00	NONE	\$688,255.00	---	---
Two (100% Survivor)	\$4,888.00	\$4,888.00	---	---	---
Three (50% Survivor)	\$5,225.00	\$2,612.00	---	---	---
Four (5& Maximum)	---	---	---	---	*
Four (5 & Maximum)	\$5,396.00	NONE	---	\$28,052.00	50%
Four (5 & Maximum)	\$5,282.00	NONE	---	\$42,078.00	75%
Four (5 & 1)	---	---	---	---	*
Four (5 & 1)	\$5,255.00	NONE	\$660,326.00	\$28,052.00	50%
Four (5 & 1)	\$5,144.00	NONE	\$646,376.00	\$42,078.00	75%
Four (5 & 2)	---	---	---	---	*
Four (5 & 2)	\$4,649.00	\$4,649.00	---	\$28,052.00	50%
Four (5 & 2)	\$4,590.00	\$4,590.00	---	\$42,078.00	75%
Four (5 & 3)	---	---	---	---	*
Four (5 & 3)	\$5,012.00	\$2,506.00	---	\$28,052.00	50%
Four (5 & 3)	\$4,906.00	\$2,453.00	---	\$42,078.00	75%
Five	\$5,167.00	NONE	---	\$56,104.00	100%

* These nontaxable contributions of \$31,579.00 will be included with this judge's excess refund due to benefits exceeding the 75% limitation (see below) and, therefore, are not included in these estimates.

** Unused sick leave credit is not included in the estimate computations.

Notes:

- Total membership service rendered as a judge.
- Excess Refund due to 75% limitation: \$164,000.00 (Nontaxable: \$31,579.00). This amount will be refunded separately to retiree.
- The difference between the nontaxable amount and the Option 4 or 5 refund is the estimated taxable amount that the retiree may rollover into an IRA or qualified plan.
- The average monthly salary used in this estimate calculation is \$7,500.00.

ADDITIONAL SERVICE CREDITS

UNUSED SICK LEAVE

An employee who retires in good standing with a minimum of 60 or more days of unused sick leave shall be entitled to additional service credit.

Sixty days of unused sick leave would increase the employee's years of service by 3 months; each additional 20 days would provide 1 more month of service credit as would any balance of 10 or more days. Any remaining balance of less than 10 days would provide no service credit.

Examples:

- (1) 70 days of unused sick leave meets the requirement of 60 days minimum

<u>70 days unused sick leave</u>	
20 days (1 month)	= 3 months (60 days)
Balance of 10 days	= <u>1 month</u>
Total	= 4 months

- (2) 85 days of unused sick leave meets the requirement of 60 days minimum

<u>85 days</u>	
20 days (1 month)	= 4 months (80 days)
Balance of 5 days	= <u>0</u>
Total	= 4 months

After determining the number of unused sick leave days, additional service credit would be calculated as previously specified.

Upon retirement, please notify your department that the audited unused sick leave and vacation forms are needed to finalize your pension.

MILITARY SERVICE CREDIT

Any member who rendered honorable active military service in the armed forces of the United States can acquire up to 4 years of membership service for the military service effective July 1, 1989 as follows:

- A member with 8 years of credited service with the Employees' Retirement System (ERS) can acquire up to 2 years of military service if hired before June 18, 1996. (ACT 136/97)
- A member with 10 years of credited service with the ERS can acquire up to 3 years of military service, if hired after June 17, 1996.
- A member with 20 years of credited service with the ERS can acquire up to 3 years of military service.
- A member with 25 years of credited service with the ERS can acquire up to 4 years of military service.

Active military service is considered service in the member's occupation at the time of purchase. Therefore, military service purchased while a judge will give the member a 3½% benefit.

The cost will be based on 7.8% of current monthly salary for each month purchased if their military service was after July 1, 1961. If service in the military was prior to that date, cost is based on 6% of current salary.

Detailed information in the military service credit booklet is available upon request.

PREVIOUSLY REFUNDED SERVICE

Previously refunded State or Country service can be purchased. You will receive 2% per year for any general employee service and 3½% per year for any judge or elected official service.

The cost to purchase this service will be based on 7.8% of current monthly salary for each month purchased if your previous employment was after July 1961. If your service was prior to that date, the cost is based on 6% of current monthly salary.

NOTE: ERS is now able to accept monies from deferred compensation plans or tax-sheltered annuity plans to purchase allowable service credits. Please be advised that each tax-sheltered institution needs sufficient time to transfer funds to the ERS. All purchases must be made prior to your retirement date.

NONCONTRIBUTORY SERVICE

Previous non-vested noncontributory plan service, which was forfeited after termination, will be acquired at no cost on a month for month basis. Service in this capacity is credited at 1.25% for retirement benefit calculation purposes.

TAXATION ON BENEFITS

OVERVIEW

The Tax Reform Act of 1986, which has been described as one of the most sweeping pieces of tax legislation in the last 30 years, changed the tax rules for members retiring from the CONTRIBUTORY retirement plan. These members must now recover their after-tax contributions to the Retirement System over their expected lifetime.

TEN PERCENT ADDITIONAL TAX RULES (Refund plans only)

A provision of the Tax Reform Act of 1986 assesses an additional 10% federal income tax on Option Four/Five refund payments made BEFORE age 55. However, if you attain age 55 anytime during the calendar year of your separation from service, you are exempt from this tax. This additional tax only applies to the taxable portion of any Option Four/Five refund payment and not the total refund payment.

The 10% additional tax, however, is not imposed on:

1. Semi-monthly pensions.
2. Payments made to members who separate from service after age 55 and elect to withdraw their contributions.
3. Payments for disability retirement.
4. Death benefit payments to a beneficiary or member's estate.

EMPLOYER PICKUP PLAN

To counteract the negative effects of the Tax Reform Act of 1986, the Employer Pickup plan was introduced by the Administration and passed by the 1987 Legislature. Major provisions of the plan that became effective January 1, 1988 are:

1. Mandatory participation by CONTRIBUTORY Plan members.
2. Deferment of federal income tax on retirement contributions.

<u>EXAMPLE</u>	
Gross Monthly Salary	\$3,000
Less Retirement Contributions (7.8%)	- 366
Subject to Federal Income Tax	\$2,634

- Effective January 1, 1999, purchases of service by payroll deduction are on a "pre-tax" basis and federal income taxes will be deferred until refunded.
 - Contributions are subject to federal income tax upon retirement or upon termination of employment if a refund is received.
3. Computation of State income tax based on gross salary.
 - No deferment since retirement benefits not subject to State income tax.
 4. Computation of retirement benefit based on gross salary.

TECHNICAL CORRECTIONS ACT OF 1988

A special amendment to the Technical Corrections Act of 1988 (HR 4333), introduced by the late Senator Spark Matsunaga, allows all employee contributions up to December 31, 1986 that are included in the Option Four/Five refund payment to be recovered tax-free in the year of payment. Therefore, contributions made in 1987 and additional lump sum purchases of service are after-tax contributions and will be recovered tax-free over the retiree's estimated lifetime.

The following simplified example illustrates the tax treatment on an Option Five refund payment up to 1988.

	<u>TOTAL EMPLOYEE CONTRIBUTIONS</u> (excluding interest)	<u>TOTAL OPTION FIVE REFUND</u> (including interest)	<u>NON TAXABLE PORTION</u>	<u>TAXABLE PORTION</u>
Up to 1986	\$48,000	\$67,000	\$48,000	\$19,000
1987	4,000*	7,000	---	7,000
1988	5,000	8,000	---	8,000
Purchase of Service (1988 & on)	<u>15,000*</u>	<u>15,000</u>	---	<u>15,000</u>
	\$72,000	\$97,000	\$48,000	\$49,000

(*These amounts will be recovered tax-free on a prorated basis and will be reflected on future federal income tax returns. There is no "double taxation" of after-tax contributions to the Retirement System.)

Effective January 1, 1993, a new tax law allows for the tax-free rollover of the taxable portion of the Option Four or Five refund payment into an IRA or another qualified plan.

If the taxable portion of the Option 4 or 5 refund is not directly rolled over at retirement by the ERS to an IRA or qualified plan, at least 20% of the taxable portion must be withheld for Federal income tax purposes. The 20% is a mandatory Federal income tax withholding. It is not a penalty or an additional tax.

Examples of the effect of the tax law on the Option Five refund payment follow:

Option Five Refund	\$97,000
Nontaxable Amount	<u>-48,000</u>
Taxable Amount	\$49,000

FULL ROLLOVER

Taxable (Check sent directly to financial institution):	\$49,000
Nontaxable Amount (Check to retiree):	\$48,000

PARTIAL ROLLOVER

Any taxable portion not rolled over is subject to the 20% mandatory income tax withholding.

Taxable	\$49,000
Rollover Amount	<u>-28,000</u>
Net Taxable	\$21,000
	<u>- 4,200</u> (20% x \$21,000 taxable)
	\$16,800
Nontaxable Amount	<u>+48,000</u>
Check to retiree:	\$64,800

NO ROLLOVER

Option Five Refund:	\$97,000
Less Federal Withholding Tax	<u>- 9,800</u> (20% x \$49,000 taxable)
Check to retiree	\$87,200

If the retiree elects a partial rollover or no rollover at retirement, all or a portion of the taxable amount can still be rolled over into an IRA or qualified plan. The rollover must be done within 60 days. Since the 20% would already have been withheld, recovery of the withholding would occur when personal income tax returns are filed.

The following illustrates the amount of income tax that may be payable if no rollover occurs. Remember that in this example, although income tax is assessed at 31%, 20% was already withheld. Therefore, only the difference would be due.

Income Tax at 31% (Maximum tax bracket) of \$49,000:	\$15,190
Retirement <u>Under</u> age 55: 10% Additional Tax on Taxable Portion	<u>4,900</u>
TOTAL TAX	<u>\$20,090</u>

The actual amount of income tax that is payable will depend upon the retiree's age and tax bracket.

RECOVERY OF NONTAXABLE CONTRIBUTIONS

Effective January 1989, the Employees' Retirement System has been using the Safe Harbor Method to determine the taxable and nontaxable portions of pension payments.

The Safe Harbor Method enables retirants to recover their nontaxable contributions over their lifetime and is based upon their age at retirement. (Age determines the number of payments and portion of the monthly benefit that is nontaxable.)

The following table illustrates this method of recovery:

<u>AGE</u>	<u>NUMBER OF PAYMENTS IF YOUR ANNUITY START DATE WAS</u>	
	<u>AFTER NOVEMBER 18, 1996</u>	<u>BEFORE NOVEMBER 19, 1996</u>
55 and under	360	300
56-60	310	260
61-65	260	240
66-70	210	170
71 and over	160	120

If your annuity start date is after 12/31/97 and is payable over the lives of more than one individual (continuing benefit), the total number of expected payments is based on the combined ages of the annuitants at the annuity starting date. (*Special Rules of the Small Business Job Protection Act of 1996 effective November 20, 1996.*)

<u>COMBINED AGES</u>	<u>NUMBER OF PAYMENTS</u>
110 and under	410
111-120	360
121-130	310
131-140	260
141 or older	210

FORMULA:

$$\frac{\text{After Tax Contributions}}{\text{Number of Payments}} \times \text{Months Retired in Calendar Year} = \text{Annual Nontaxable Portion}$$

EXAMPLES:

Illustrations calculating the nontaxable portion of a 55 year old retirant's pension payments using the above formula and the After-Tax Contribution amounts as follows:

1. Option 5

Refund: \$97,000 (\$48,000 nontaxable)

$$\text{Exemption: } \frac{\$4,000 + \$15,000}{360 \text{ payments}} \times 12 \text{ Months} = \$633 \text{ annual nontaxable portion}$$

Therefore, in this example, if the retirant receives an annual pension of \$18,000, \$633 is nontaxable and the balance of \$17,367 is subject to federal income tax until the full after-tax contributions of \$19,000 are recovered. At that point, the entire annual pension of \$18,000 is taxable.

2. Maximum Allowance; Options One, Two and Three

Refund: None

$$\text{Exemption: } \frac{\$48,000 + \$4,000 + \$15,000}{360 \text{ payments}} \times 12 \text{ months} = \$2,233 \text{ annual nontaxable portion}$$

Therefore, in this example, if the retirant receives an annual pension of \$31,000, \$2,233 is nontaxable and the balance of \$28,767 is subject to federal income tax until the full after-tax contributions of \$67,000 are recovered. At that point, the entire annual pension of \$31,000 is taxable.

Since these options do not have a refund of contributions, the nontaxable pre-1987 contributions of \$48,000 are included in the recovery computation.

**If the annuity is based on a continuing benefit (option 2,3,4(2), 4(3), and started after 12/31/97, the number of payments would be based on the combined ages of the annuitants.*

FREQUENTLY ASKED TAX QUESTIONS

1. *Are my retirement benefits subject to State of Hawaii taxes?*

No, all benefits paid by ERS are nontaxable for State purposes.

2. *If I do not select Option Four or Five, why am I being taxed on my "own" money that was already taxed when I was working?*

The Tax Reform Act of 1986 eliminated the "three year basis recovery rule" which enabled members to defer tax payments until they recovered their contributions to the ERS. Under the current law, you can only recover your after-tax contributions over your lifetime.

3. a) *What happens if I should die before I recover my own contributions?*

For those members who retire after July 1, 1986, your beneficiary or estate may recover the cost by amending your tax returns for the previous three years and carrying the unrecovered cost forward for fifteen years if necessary.

- (b) *Are my death benefits taxable to my beneficiaries or estate?*

Yes. Prior to August 20, 1996, regulations allowed a beneficiary or estate of a deceased employee to exclude up to \$5,000 from income taxes. The Small Business Job Protection Act of 1996 repeals this exclusion for deaths occurring after August 20, 1996.

4. *Can I rollover the taxable portion of my Option Four or Five refund payment into an Individual Retirement Account (IRA)?*

Yes. Effective January 1, 1993, the taxable portion of an Option Four or Five refund payment can be rolled over into an IRA or another qualified plan. Death benefits to a surviving spouse and refund payments to terminating employees who forfeit retirement benefits, can also be rolled over.

Members should seek the advice of a financial consultant or call the applicable qualified plans or administrator of the IRAs, to determine if the plan they are interested in is qualified.

5. *Can I rollover the taxable portion of my Option 4 or 5 refund payment to my tax deferred compensation or tax sheltered annuity (TSA or TDAs) plans?*

No. Since you will be retired, you are not allowed to rollover funds to tax deferred compensation or tax sheltered annuity plans under the current provisions of the Internal Revenue Code.

6. *After I retire, how will I know the taxable amount that I need to pay the IRS?*

ERS will calculate the taxable amount of your pension and mail you the appropriate tax form by January 31 of each year with information necessary to file your federal income tax return.

ORDINARY DEATH BENEFIT

Contributory Plan

In the event of death of a member while in service (active employment) from any cause other than an accident in the performance of duty, the designated beneficiary receives the (1) return of retirement contributions and interest and (2) percentage of the salary paid in the 12 months immediately preceding death.

The members of this group must meet the same minimum requirements to qualify for ordinary death benefits as other employees of the contributory plan.

Since eligibility for the Option 2 (100% Joint Survivor) benefit is dependent upon whether a member qualifies for retirement, members under age 55 who are eligible for the 3½% benefit only need a minimum of 10 years of service. Ordinary death benefits are payable even if death occurred while on authorized leave without pay.

<u>Percentage</u>	<u>Years of Service</u>
50%	1-10
5%	Each additional full year in excess of 10 years
100%	Maximum 20 years

Example: IN SERVICE AT TIME OF DEATH

SERVICE: 28 years 10 months

BENEFIT PAYABLE

SALARY EARNED IN YEAR PRECEDING DEATH (100% based on 28 years 10 months)	\$106,921.00
RETURN OF CONTRIBUTIONS (including accrued interest)	<u>\$220,000.00</u>
TOTAL	\$326,921.00

In lieu of the ordinary death benefit, the beneficiary may elect an Option Two benefit if the member was eligible for service retirement. If the member had 10 or more years of credited service but was ineligible for service retirement, the beneficiary may elect an Option Three benefit. Death payments will start on the first of the month preceding the date of death.

Options Two or Three are only available if one beneficiary was designated. If the member designated multiple beneficiaries, only the ordinary death benefit will be payable. If Options Two or Three are selected, the surviving spouse and dependent children under age 19 may be eligible for benefits under the Hawaii Employer-Union Health Benefits Trust Fund (EUTF). Please contact the EUTF at 586-7390 for more information.

It is very important that the member's beneficiary designation on the Employees' Retirement System's Form 1A (Designation of Beneficiary) be in order. By law, the designation becomes null and void whenever the members' marital status changes or the designated beneficiary dies. If the beneficiary designation is not updated when either of these situations occurs, a recent amendment to the law now enables the surviving spouse, reciprocal beneficiary, or dependent children to receive benefits. The surviving spouse or reciprocal beneficiary can elect Option Two if the member was eligible for service retirement, Option Three if the member had 10 or more years of credited service but was ineligible for service retirement, or a lump sum ordinary death benefit. If there is no surviving spouse or reciprocal beneficiary, dependent children under age 18 can receive the lump sum ordinary death benefit without going through probate.

Benefits under the Hawaii Employer-Union Health Benefits Trust Fund (EUTF) may be provided for active deaths for members even if death occurred while on authorized leave without pay. Please contact the EUTF directly at 586-7390 for more information

CONTRIBUTORY PLAN COMPARISON CHART

	JUDGES, Elected Officials, & Legislative Officers	General Employees	Police, firefighters, investigators of the Attorney General's Office, & Adult Corrections Officers
CONTRIBUTIONS	7.8% (of salary)	7.8% (of salary)	12.2% (of salary)
PENSION BENEFIT (Calculation formula)	3 ½% X Years of Service X AFC*(plus annuity)	2% X Years of Service X AFC	2 ½% X Years of Service X AFC
ANNUITY (on retirement contributions)	Yes	No	No
MINIMUM AGE FOR RETIREMENT	None (10 years of service if hired prior to June 30, 1999). After June 30, 1999, any member who first earned credited service as a judge may retire at age 55 with 5 years of service or any age with 25 years of service.	<ul style="list-style-type: none"> • Age 55 with 5 years of service or • None with 25 years of service (age reduction penalty if under age 55). 	<ul style="list-style-type: none"> • Age 55 (with 5 years of service) or • None with 25 years of service. (no age reduction penalty if service in this capacity)
ORDINARY DISABILITY RETIREMENT	3 ½% pension calculation benefit plus annuity	1¾% with a minimum of 30% of the AFC	1 ¾% with a minimum of 30% of the AFC

* AFC refers to the Average Final Compensation (commonly known as the “high three” or “high five”).

Other 3½% PENSION CALCULATION BENEFIT FORMULA GROUPS

- **ELECTED OFFICIALS** – Optional for State and County government elected officials. Category includes governor, lieutenant governor, mayors, legislators, council members, and the prosecuting attorney for each county.
- **LEGISLATIVE EMPLOYEES** – Chief clerks, assistant clerks, sergeant-at-arms, of both houses of the Legislature.

ERS OFFICE LOCATIONS & PHONE NUMBERS

The Employees' Retirement System (ERS) headquarters is located on the corner of Merchant and Alakea Streets on the 14th floor of the City Financial Tower in downtown Honolulu. Validated parking is available in the building. City Financial Tower parking entrance is on Richards Street.

Office hours are from 7:45 a.m. to 4:30 p.m. Monday through Friday (except holidays)

OFFICES:

Oahu

Employees' Retirement System
City Financial Tower
201 Merchant Street, Suite 1400
Honolulu, HI 96813

Benefits Branch: 586-1735
Fax: (808) 587-5766

Hawaii

Hawaii District Office
101 Aupuni Street, Suite 203
Hilo, HI 96720

(808) 974-4077 or
Toll-free to Oahu @ 974-4000 Ext. 61735

Kauai

Kauai District Office
3060 Eiwa Street, Room 302
Lihue, HI 96766

(808) 274-3010 or
Toll-free to Oahu @ 274-3141, Ext. 61735

Maui

Maui District Office
54 High Street, Room 218
Wailuku, HI 96793

(808) 984-8181 or
Toll-free to Oahu @ 984-2400, Ext. 61735

Molokai/Lanai

Toll-free to Oahu @ 1-800-468-4644, Ext. 61735

US Mainland Only

Toll-free to Oahu @ 1-888-659-0708

You may also visit our Website at www2.hawaii.gov/ers for general information.

EMPLOYEES' RETIREMENT SYSTEM

Pre-Retirement Orientation

REQUEST FOR INFORMATION

Please complete the form below. It will help us review your records and provide you with answers.

Name: _____ SSN: _____
Address: _____ Phone: (Bus) _____
_____ (Home) _____
_____ (Cellular) _____

Have you previously filed a retirement application? Yes ☐ No ☐

I would like to request the following information:

Signature: _____ Date: _____